

D.P.U. 96-25-A

Petition of Massachusetts Electric Company and Nantucket Electric Company, pursuant to General Laws Chapter 164, §§ 76 and 94, and 220 C.M.R. §§ 1.00 et seq., for review of its electric industry restructuring proposal.

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I. INTRODUCTION

On February 26, 1997, the Department of Public Utilities ("Department") approved an offer of settlement ("Settlement") of electric industry restructuring issues, including the provisions of a wholesale rate stipulation and agreement ("Wholesale Settlement") submitted by Massachusetts Electric Company ("MECo") and Nantucket Electric Company ("Nantucket") (together, "Companies").¹ Massachusetts Electric Company, D.P.U. 96-25 (1997). In D.P.U. 96-25, the Department reviewed provisions that were a condition of the Settlement.² The Department also noted that approval of the Settlement was conditioned on Federal Energy Regulatory Commission ("FERC") approval of the provisions of the Wholesale Settlement as filed with the FERC on December 3, 1996.³ The Department further noted that FERC approval of a Wholesale Settlement other than as filed with the FERC would require the Settlement to be resubmitted for Department review. D.P.U. 96-25, at 31. On May 28, 1997,

¹ The original Settlement was submitted to the Department on October 1, 1996. On January 14, 1997, the Company submitted amendments to the Settlement intended to address concerns raised by the Department ("January 14, 1997 Amended Settlement"). On February 13, 1997, the Company submitted revisions to the January 14, 1997 Amended Settlement intended to address concerns raised by members of the Massachusetts Legislature.

² On May 8, 1997, the Department issued an Order on provisions that were not a condition of the Settlement. Massachusetts Electric Company, D.P.U. 96-25 (Phase II) (1997). In addition, on June 13, 1997, the Department initiated a proceeding to develop model terms and conditions governing the relationships between distribution companies and customers, and distribution companies and competitive suppliers. Notice of Inquiry and Order Seeking Comments on Model Terms and Conditions for Distribution Companies, D.P.U. 97-65 (June 13, 1997). See ' V. at 23-24, below.

³ See Docket No. ER97-678-000 for New England Power Company ("NEP"), the Companies' wholesale affiliate; see also, Docket No. ER97-680-000 for NEP's Rhode

New England Power Company ("NEP") submitted an amended wholesale stipulation and agreement ("Amended Wholesale Settlement") to the FERC for review,⁴ and the Companies filed an amended offer of settlement ("Amended Settlement"),⁵ which includes the Amended Wholesale Settlement, with the Department for review. In addition, in compliance with D.P.U. 96-25, the Companies submitted revised unbundled and retail delivery tariffs. See also Massachusetts Electric Company, D.P.U. 97-45 (1997).⁶

Island retail affiliate, Narragansett Electric Company.

⁴ The Department is a party to the FERC proceeding, but not a signatory to the Amended Wholesale Settlement.

⁵ The Department marks the Amended Settlement as Exhibit Meco-11. The amended offer of settlement is volume 1, the wholesale offer of settlement is volume 2, the wholesale offer of settlement, marked to show changes is volume 3, the compliance unbundled 1997 tariffs are contained in volume 4, and the compliance retail delivery 1998 tariffs are contained in volume 5.

⁶ On March 3, 1997. the Companies submitted unbundled and retail delivery tariffs in

Pursuant to notice duly issued, the Department received both initial and reply comments on the Amended Settlement. Enron Capital & Trade Resources and Wheelabrator Environmental Systems, Inc. filed initial comments on June 11, 1997. The Companies and the Attorney General filed reply comments on June 18, 1997. This Order reviews the Amended Settlement in the context of the Settlement approved by the Department in D.P.U. 96-25.

compliance with the Department's directives in Electric Industry Restructuring Plan: Model Rules and Legislative Proposal, D.P.U. 96-100 (1996). In D.P.U. 97-45, the Department disallowed the March 3, 1997 tariff filings as not consistent with the directives of D.P.U. 96-25.

II. DESCRIPTION OF THE SETTLEMENT APPROVED IN D.P.U. 96-25

The Settlement represents a comprehensive company-specific resolution of issues relating to electric industry restructuring including (1) the unbundling of the Companies' existing tariffs, (2) customer choice, with standard offer and universal service provisions, (3) near-term rate reductions, (4) low-income customer protections, (5) recovery of stranded costs, (6) divestiture of generating facilities, (7) improved environmental performance, and (8) continued funding for demand-side management ("DSM") programs. D.P.U. 96-25, at 6.

Under the Settlement, the Companies will implement unbundled rates for their customers prior to the date that retail customer choice in a competitive generation market becomes available to customers of investor-owned electric companies in Massachusetts, the retail access date. Id. citing Exh. MECo-10, at 5-6. The retail access date would be the later of January 1, 1998, or the date when access to competitive generation suppliers is made available to all customers of investor-owned electric companies in Massachusetts. As of January 1, 1998, MECo could also seek Department approval to implement retail access for its customers prior to the date when retail access is made available to customers of other investor-owned electric companies in Massachusetts. Id. at 7, n.11, citing Exh. MECo-10, at 22.

MECo's unbundled rates will be divided into delivery service charges and energy service charges. Id. at 7, citing Exh. MECo-10, at 5-6. The delivery service charges cover distribution costs, including conservation cost factors, an allowance for transmission costs and recovery of fixed costs associated with NEP's purchased power expense currently recovered under the existing tariff. Id. The energy service charges will include MECo's fuel clause plus

an allowance equal to the variable energy costs currently recovered under the existing tariff.

Id. MECo would roll a Purchased Power Cost Adjustment ("PPCA") factor, with a reconciliation adjustment, into base rates and eliminate future PPCA adjustments. Id. The fuel clause adjustment will continue as a reconciling adjustment until the retail access date. Id.

On the retail access date, the Company will implement retail delivery tariffs. Id. citing Exh. MECo-10, at 7. The retail delivery rates will include four components: (1) distribution charges, including performance standards for reliability and customer satisfaction,⁷ that would be effective until January 1, 2001; (2) transmission charges that recover, on a reconciling basis, transmission service provided by NEP, and any other charges billed to the Companies for transmission service; (3) an access charge designed to recover costs associated with termination of the all-requirements contract that the Companies have with NEP; and (4) an energy charge for the generation component. Id. at 7-8, citing Exh. MECo-10, at 7-8. The retail delivery tariffs of the Settlement unbundle the transmission charge from the distribution and access charges, and provide for a separate transmission service cost adjustment, which does not apply to retail customers that arrange for transmission service separately from MECo. Id. at 8, citing Exh. MECo-9, at 7. The transmission and distribution charges are based on the existing separation of distribution and transmission facilities. In the event that facilities or costs are transferred, appropriate adjustments to the transmission and distribution components would reflect the transfer. Id. at 8, n.15, citing Exh. MECo-10, at 10. The Settlement also provides

⁷ The Companies will credit customers' bills when the duration of outages exceeds 105 minutes per customer per year or the level of customer satisfaction, as determined by customer surveys, is below 85 percent. Id. at 7, citing Exh. MECo-1, vol. 3, at 38-39.

that, effective January 1, 2000, the Companies will file a proposal with the Department to unbundle distribution services that can be provided competitively, without impairing system reliability or other system benefits. Id. at 7, n.12, citing Exh. MECo-10, at 36.

The Companies will provide standard offer service for all of their customers who do not choose a competitive generation supplier on the retail access date. Id. at 8, citing Exh. MECo-10, at 4. The generating supplies for standard offer service will be obtained by the Companies through a competitive solicitation. Id. at 8, citing Exh. MECo-10, at 15. The Companies will provide standard offer service to retail customers at fixed prices increasing from 2.8 cents per kilowatthour ("KWH") on the retail access date to 5.1 cents, subject to a fuel price index which takes effect after January 1, 2000, during a transition period from the retail access date through December 31, 2004. Id. at 9, citing Exh. MECo-10, at 8. Pursuant to the Wholesale Settlement, NEP has proposed to provide the Companies with a generating supply for standard offer service at fixed prices increasing from 3.2 cents per KWH on the retail access date to 5.1 cents per KWH, subject to the fuel price index, during a transition period from the retail access date through December 31, 2004. Id. at 9, n.17, citing Exh. MECo-1, vol. 2, at 12. NEP may bid in the solicitation at prices less than its proposed standard offer supply. Id. at 9, n.17, citing Exh. MECo-1, vol. 2, at 14. Because the generation supply will be determined through a competitive solicitation and the Companies' standard offer prices are guaranteed, the Companies will reconcile the revenues received from retail customers taking the standard offer with payments to suppliers through an adjustment on standard offer customer bills. Id. at 9, n.19, citing Exh. MECo-10, at 16-17.

Once a competitive supplier is selected, a customer may not return to standard offer service, with the exception that during the first year after the retail access date, residential and G-1 customers that have taken service from a competitive supplier may return to standard offer service within ninety days of the selection of a competitive supplier. Id. at 9, citing Exh. MECo-10, at 15. Under the safety-net and basic service provisions of the Settlement, the Companies will continue to deliver electricity to consumers who are no longer eligible for standard offer service because they have chosen a competitive supplier, and who do not receive service from the competitive supplier, at rates approved by the Department. Id. at 9, citing Exh. MECo-10, at 17-18.

The retail delivery rates, with the standard offer service option, are designed to provide an initial ten percent rate reduction to all customers. Id. at 9, citing Exh. MECo-10, at 9; Exh. MECo-7. The value of the ten percent rate reduction will be maintained by capping average revenues per KWH from retail delivery service, including the standard offer, at 8.91 cents per KWH, adjusted for the Consumer Price Index, excluding (1) the fuel price index, (2) adjustments caused by the return on equity floor, and (3) tax law or accounting changes. Id. at 9-10, citing Exh. MECo-10, at 18-19. The Companies will defer amounts necessary to meet the cap and recover the deferrals subject to reductions in the contract termination charge ("CTC"), explained below. Id. at 10, citing Exh. MECo-10, at 19.

Regarding protections for low-income customers, the Companies will continue the low-income discount, and will fund low-income customer DSM programs. Id. at 10, citing Exh. MECo-10, at 27. In addition, for low-income customers who have chosen a competitive

supplier, the Companies will implement a program to protect against redlining by paying market suppliers directly, up to the price of the standard offer. Id. The Companies would include any unrecovered cost for this service and the low-income discount in the distribution charge. Id.

On the retail access date, the Companies would terminate their all-requirements contract with NEP,⁸ and would pay NEP the CTC to provide for NEP's recovery of its stranded costs. Id. at 10-11, citing Exh. MECo-10, at 4-5. NEP would recover the Companies' proportionate share, 72.6 percent, of NEP's total contract termination costs. Id. at 11, citing Exh. MECo-1, vol. 2, at 6. The Companies collect the CTC through an access charge that will apply to all KWH delivered to consumers of electricity in the Companies' service area who receive distribution service, whether or not they are currently customers of the Companies.⁹ Id. The Companies would enter into a network integration transmission service agreement with NEP for transmission service under NEP's open access transmission tariff. Id. at 11, n.23, citing Exh. MECo-1, vol. 2, at 10. The network integration transmission service agreement incorporates the CTC provision, and in the event the Companies are denied the ability to recover the CTC

⁸ NEP's rates would remain in effect for service to the Companies through the earlier of December 31, 2000, or termination of the all-requirements contract. The contract termination date is defined as the earlier of the retail access date or the date, not before January 1, 1998, on which the Companies terminate purchases under the all-requirements contract. As of the contract termination date, NEP would have no further obligation to meet the electricity demand of the Companies, except as provided by a separate agreement to provide standard offer service. Id. at 11, n.22, citing Exh. MECo-1, vol. 2, at 14).

⁹ The wholesale rate stipulation and agreement excludes the Massachusetts Bay Transportation Authority accounts, for which MECo currently provides unbundled distribution service. Id. at 11, n.24, citing Exh. MECo-1, vol. 2, at 6, citing FERC Docket ER94-129-000.

from their customers in the access charge for distribution service, NEP proposes to collect the unrecovered balance as a surcharge on any rate paid for transmission service to the Companies' service area. Id. at 11, n.23, citing Exh. MECo-1, vol. 2, at 11.

The CTC will be capped at 2.8 cents per KWH, and will be composed of both fixed and variable components. Id. at 11, citing Exhs. MECo-10, at 8; MECo-1, vol. 2, at 48-61. The fixed component of the CTC will recover the Companies' allocated share of NEP's costs for (1) revenues sufficient to amortize (over a twelve-year period) generating plant balances and regulatory assets; (2) revenues sufficient to provide an overall pre-tax return of 11.18 percent (based on a combined state and federal income tax rate of 39.225 percent); (3) transmission wheeling charges, at prescribed levels, associated with NEP's entitlement to off-system purchases; and (4) the costs, independent of operation, of NEP's entitlement in Maine Yankee, Vermont Yankee, Millstone 3, and Seabrook, representing operations and maintenance expenses and property taxes for these units that would be incurred prior to the earlier of December 31, 2009 or the expiration of the operating licenses for these units, assuming that these units were to cease operating on December 31, 1997. Id. at 11, n.25, citing Exh. MECo-1, vol. 2, at 48-53.

The variable component of the CTC will recover the Companies' allocated share of NEP's costs for (1) nuclear decommissioning and site restoration costs; (2) above-market payments to power suppliers under existing contracts, less the market value realized from the resale of electricity purchased under these contracts; (3) purchased power contract economic buyout payments; (4) credit for unit sales contracts; (5) above-market fuel transportation costs;

(6) payments in lieu of property taxes; (7) employee severance and retraining costs; (8) damages, costs or net recoveries from claims by or against third parties associated with NEP's generating business accrued prior to the date of divestiture; and (9) performance-based rates for nuclear units remaining after divestiture. Id. at 11, n.25, citing Exh. MECo-1, vol. 2, at 53-61. The variable component will be adjusted through a reconciliation mechanism for differences between estimates of the Company's allocated payments and actual payments. Id. at 11, n.25, citing Exh. MECo-1, vol. 2, at 54.

The Settlement provides that NEP will file a plan with both the Department and the FERC to implement a divestiture of generation facilities, including NEP's generation facilities, properties owned by New England Energy Inc., the generating units of Nantucket, and the Narragansett Electric Company's ownership interest in the Manchester Street Station. Id. at 12-13, citing Exhs. MECo-10, at 29-30; MECo-1, vol. 2, at 15. The Settlement provides that NEP will also file a plan with the Department to separate its generating business from its transmission business. Id. at 13, n.27, citing Exh. MECo-10, at 29.

As part of the divestiture, NEP will endeavor to sell, lease, assign, or otherwise dispose of minority shares of nuclear units or entitlements, subject to Nuclear Regulatory Commission approval. Id. at 13, citing Exh. MECo-10, at 29-30. In the event NEP is unable to divest its nuclear generating units or entitlements, it would implement a performance-based rate to cover the costs of their continued operation. Id. at 13, citing Exh. MECo-10, at 30-31. NEP would also endeavor to sell, assign or otherwise dispose of its purchased power contracts. Id.

To facilitate the divestiture of NEP's generating facilities, the Settlement provides that

NEP may seek FERC approval of market prices for wholesale electricity sales and may make an application for Public Utility Holding Company Act exempt wholesale generator ("EWG") status. Id. at 13, citing Exh. MECo-10, at 34. Approval of the Settlement constituted a finding by the Department that the participation of NEP in the market and the designation of each of its facilities as an EWG will benefit consumers, are consistent with existing state laws, will not provide any unfair competitive advantage as a facility owned or formerly owned by NEP, and are in the public interest. Id. at 13, n.28, citing Exh. MECo-10, at 34-35.

NEP will apply a residual value credit from the proceeds of the divestiture as a direct offset to the CTC. Id. at 13, citing Exh. MECo-1, vol. 2, at 7. The Wholesale Settlement contains an informal dispute resolution procedure to resolve disputes about the calculation of the residual value credit and CTC, and provides for petition to the FERC if a dispute is not resolved informally. Id. at 13, n.29, citing Exh. MECo-1, vol. 2, at 7-8. In order to reduce the CTC by mitigation efforts, the Settlement includes a mitigation incentive mechanism, which would allow NEP to retain a portion of reductions in the CTC, and which, through the reconciliation adjustment, would increase the variable component of the CTC when the unadjusted CTC is reduced below the 2.8 cents per KWH cap. Id. at 13, citing Exh. MECO-1, vol. 2, at 55.

Regarding improved environmental performance, the Settlement also commits NEP, or its successors, to nitrogen oxide and sulphur dioxide emissions reductions at its Brayton Point and Salem Harbor generating facilities. Id. at 14, citing Exh. MECo-10, at 24. At the same time, the Settlement does not restrict environmental regulators' authority to impose new

environmental standards. Id.

Finally, concerning continued DSM funding, the Settlement provides that the Company will develop budgets for DSM programs and renewables for the period 1998 through 2001 at \$66.7 million annually, adjusted for outstanding energy conservation services and conservation cost factors on the retail access date. Id. The DSM programs will include low-income customer residential programs, and the Settlement will provide funding to develop fuel cells and renewables. Id. The Department would decide the appropriate funding level for ongoing DSM programs and renewables after December 31, 2001. Id. at 14, citing Exh. MECo-10, at 25.

III. CHANGES TO THE SETTLEMENT APPROVED IN D.P.U. 96-25

The Amended Settlement contains several modifications to provisions of the Settlement approved in D.P.U. 96-25.¹⁰ The Settlement contained a provision to establish a storm fund to pay for the incremental restoration costs, over \$1,000,000, of any major storm occurring after the date the Settlement is approved (Exh. MECo-11, vol. 1, at 9, n.4). The Amended Settlement provides for a five-year amortization of the restoration costs for a storm MECo experienced prior to the approval of the Settlement which led to incremental restoration costs of over \$7,000,000 (id.). This amount is net of a credit to the initial balance of \$2,145,000 representing MECo's share of NEP's estimated costs associated with employee severance and

¹⁰ The Amended Settlement and Amended Wholesale Settlement also state that the Utility Workers Union of America, Local 464, Utility Workers Union of America, AFL-CIO, and Massachusetts Alliance of Utility Unions, intervenors in the Department's proceeding, do not oppose the agreement. In addition, the Unions have withdrawn their appeal of the Department's Order in D.P.U. 96-25. See Notice of Withdrawal of Appeal, SJ-97-0210 (May 20, 1997).

retraining associated with efficiency gains from retail operations (id.). The Amended Settlement also allows residential and small commercial and industrial customers 120 days to switch from an alternative supplier back to standard offer service (id. at 16). In addition, the Amended Settlement establishes October 1, 1997 as the date by which NEP would submit its divestiture plan and a plan to separate its generating business from its transmission business (id. 30).

The Amended Wholesale Settlement reflects the changes to the Wholesale Settlement that resulted from discussions in the context of the FERC proceeding. In addition to changes intended to clarify the language of the Wholesale Settlement, the Amended Wholesale Settlement includes the following substantive modifications.

With respect to the divestiture of NEP's generating facilities, the Amended Wholesale Settlement provides that in the event that the approvals necessary for the divestiture of NEP's non-nuclear generating facilities are received prior to the retail access date, NEP would be authorized to proceed with the divestiture, and MECo would declare the wholesale access date, pay the CTC, receive any residual value credit, and obtain supplies for standard offer service from NEP (Exh. MECo-11, vol. 2, at 27, n.4). The Amended Wholesale Settlement does not require MECo to solicit competitive suppliers for standard offer service except as it relates to customer service after the retail access date (id.). In addition, during the period between the wholesale access date and the retail access date, MECo would be authorized to implement the retail delivery rates, transmission charges, and access charges without implementing retail access, and to recover the cost of purchased power for standard offer service without deferral (id.).

The Amended Wholesale Settlement allows for NEP to adjust the residual value credit to reflect the annual effect of refinancings, repurchases, and retirements of securities following divestiture or securitization associated with the implementation of the CTC (id. at 58). This adjustment would apply to the period following the divestiture date, whether or not securitization has been implemented (id.). The Amended Wholesale Settlement also provides that NEP would implement the residual value credit within three months of the sale of any, or all of its generating facilities, or any other property subject to divestiture (id. at 55). The Amended Wholesale Settlement provides for a residual value credit where a sale of assets, whose costs have been included in the CTC, occurs after December 31, 2009, the CTC recovery period (id. at 57).

The Amended Wholesale Settlement provides that NEP would require purchasers of its generating business to pay \$85 million of the costs associated with the adjustment of the workforce of NEP or its affiliates in connection with the implementation of retail access, divestiture, or the termination of NEP's all-requirements contract (id. at 66-67). In the event that the actual costs incurred by NEP or its affiliates are less than the \$85 million cap, NEP would reflect the difference in the reconciliation account (id. at 67).

In the event that NEP is unable to divest of its nuclear units or entitlements, the Amended Wholesale Settlement provides that reasonable going forward costs of operating the units and for supporting entitlements, including variable costs and capital additions, would be recovered by NEP on a cost-of-service basis (id. at 28). NEP would also encourage and support a procedure for maintaining a detailed early shutdown plan at each nuclear unit in

which it has an entitlement (id. at 29). With respect to the sale, assignment, disposition, or buydown of above-market power supply contracts,¹¹ the Amended Wholesale Settlement provides that economic buyout payments would be recovered as incurred by NEP to the extent that recovery does not increase rates to customers above the level that would have been incurred absent the sale, assignment, disposition, or buydown of such contracts (id. at 63). Any portion of the economic buyout payment that NEP would not recover as a consequence of this constraint would be deferred, with a return, and recovered as soon as recovery would not violate the constraint (id.).

The Amended Wholesale Settlement includes certain changes in the formula for the calculation of the CTC. Specifically, the Amended Wholesale Settlement modifies both the fixed and variable components of the CTC. The Amended Wholesale Settlement shifts nuclear costs independent of operation from the fixed component to the decommissioning costs portion of the variable component (id. at 52, 61). The Amended Wholesale Settlement also shifts the following from the fixed component to the variable component: transmission wheeling charges not assigned to a purchaser of the unit, associated with NEP's entitlement in Connecticut Yankee, Maine Yankee, Millstone 3, Wyman Unit 4, Vermont Yankee; and NEP's slice of the Northeast Utilities system, together with support payments to Central Maine Power and

¹¹ The Amended Wholesale Settlement removes projects that did not enter service from the list of long-term supply contracts subject to above-market payments.

Connecticut Light and Power (id. at 51, 66).

The Amended Wholesale Settlement removes the FAS 106 (post-retirement benefits other than pensions) transition obligation of NEP from the regulatory assets for generation related unrecovered net book balances and includes this amount as a separate item in the fixed component of the CTC (id. at 49, 51). The Amended Wholesale Settlement also includes an adjustment to the fixed component to be made following the divestiture date and at the time of implementation of the residual value credit, to reflect the unrecognized transition obligation, prior service cost, and unrecognized gains or losses associated with the FAS 106 and FAS 87 (pension benefits) estimated obligations (id. at 51). The gains or losses associated with FAS 87, however, would be recognized only to the extent that they exceed five percent of the greater of plan assets or liabilities (id. at 52). In addition, the Amended Wholesale Settlement includes an adjustment to the fixed component of the CTC to reflect the difference between the actual New England Energy Incorporated ("NEEI") loss and estimated NEEI loss upon the sale of NEEI properties (id. 53).

With respect to damages, costs, or net recoveries from claims by or against third parties, the Amended Wholesale Settlement provides for recovery by NEP in the reconciliation account of environmental response costs that were not assigned to NEP's successors in interest, recovered from NEP's insurance carriers, or the result of gross negligence relating to waste from divested generating facilities off the site of the properties sold, whether or not the material is regulated under the current statutes (id. 67, 69).

The Amended Wholesale Settlement provides that any adjustments made to the

reconciliation account prior to January 1, 2001 that would otherwise cause the CTC to increase or decrease by more than 0.2 cents per KWH would be amortized, with a return, over the three years following January 1, 2001 (id. at 60).

III. COMMENTS ON THE AMENDED SETTLEMENT

Wheelabrator raises a concern similar to the issue it has raised in the FERC proceeding, and had previously raised in the Department's review of the Settlement. Specifically, Wheelabrator is seeking adequate assurance that funds will be available to pay NEP's obligations under the existing power supply contracts (Wheelabrator Comments at 1). Wheelabrator recommends that the structure of the variable component of the access charge be modified to establish a trust, similar to the employee severance and retraining account, to be held for power producers and other suppliers, and that the trust should be funded by NEP in the amounts of NEP's obligations for power supply contracts (id. at 2). In addition, Wheelabrator contends that the timing of payments of the variable component proceeds is not addressed (id. at 3). In the alternative, Wheelabrator requests that this issue be deferred to and considered with hearings on the divestiture plan (id. at 2).

In its comments, Enron raises a concern relative to the variable component of the CTC. Specifically, Enron notes that the Amended Wholesale Settlement provides that reconciliation account adjustments occurring prior to January 1, 2001 that would otherwise cause the CTC to increase or decrease by more than 0.2 cents per KWH would be amortized, with a return, over the three years following January 1, 2001 (Enron Comments at 2). Enron contends that this exacerbates its concern that the Amended Wholesale Settlement contains no provisions for a

change in the variable component through January 1, 2001 (id.). Enron requests that the Department require that the Amended Wholesale Settlement be revised to allow for reconciliation of the variable component either quarterly or annually, beginning in 1998 (id. at 2-3).

The Companies replied that both Enron and Wheelabrator reargue positions settled by the Department, and that the recent amendments to the Settlement do not affect the Department's resolution of these issues (Companies Comments at 1). With respect to Wheelabrator's concern, the Companies state that approval of the Amended Settlement would not preclude the Department from undertaking the review of NEP's and the Companies' financing arrangements that is contemplated by D.P.U. 96-25, and that Wheelabrator's issues can be considered along with the interest of customers, investors, creditors, and other suppliers (id. at 2-3). The Companies state that both NEP and the Companies are subsidiaries of a registered public utility holding company, and their financings are regulated by the Securities and Exchange Commission rather than by the FERC (id. at 3, n.3). In addition, the Companies state that both NEP and the Companies are subject to the Department's jurisdiction under state law (id.). See G.L. c. 164, ' ' 14, 15, 15A, and 17A.

With respect to Enron's concerns, the Companies state that the proposed reconciliations are inconsistent with the rate stability features of the Settlement, and that Enron's proposal would destabilize one of the elements integral to the overall rate reduction (id. at 3). The Companies contend that the modification in the Amended Settlement limiting changes in the reconciliation adjustment to 0.2 cents per KWH furthers the rate stability objective, and

provides grounds for not including a reconciliation adjustment until January 1, 2001 (id.).

In reply comments, the Attorney General contends that Enron and Wheelabrator have not raised any issues of merit, and requests that the Department approve the Amended Settlement (Attorney General Comments at 1). With respect to the concern raised by Enron, the Attorney General states that the limitation on reconciliation account adjustments will ensure that any deferred reduction is delivered to consumers, with interest, while negating the possibility of an unnecessary and disruptive price swing (id. at 1-2). The Attorney General states that the concern raised by Wheelabrator amounts to a modification to the agreement that would suit its particular interest and should be rejected (id. at 2).

IV. STANDARD OF REVIEW

In assessing the reasonableness of an offer of settlement, the Department must review the entire record as presented in a company's filing and other record evidence to ensure that the settlement is consistent with Department precedent and the public interest. Berkshire Gas Company, D.P.U. 96-92, at 8 (1996); Boston Gas Company, D.P.U. 96-50, at 7 (Phase I) (1996); Massachusetts Electric Company, D.P.U. 96-59, at 7 (1996). A settlement among the parties does not relieve the Department of its statutory obligation to conclude its investigation with a finding that a just and reasonable outcome will result. Essex County Gas Company, D.P.U. 96-70, at 5-6 (1996); Fall River Gas Company, D.P.U. 96-60, at 5 (1996).

In D.P.U. 96-25, at 20, the Department stated that in assessing whether an electric company's proposed settlement of restructuring issues is consistent with Department precedent, the Department will consider whether the settlement is consistent with the overall goal and

principles for restructuring that were established in Electric Industry Restructuring, D.P.U. 95-30 (1995), and affirmed in Electric Industry Restructuring Plan: Model Rules and Legislative Proposal, D.P.U. 96-100 (1996). A settlement's consistency with our goal and principles for restructuring will ensure an outcome that is, on balance, a just and reasonable resolution of restructuring issues for an electric company and its ratepayers, and thus, in the public interest.

V. ANALYSIS AND FINDING

In D.P.U. 96-25, at 31, the Department found that the provisions of the Settlement that were a condition of its approval were consistent with (1) our primary objective to reduce costs, over time, for all consumers of electricity, (2) our goal to develop an efficient industry structure and regulatory framework that minimize costs to consumers while maintaining safe and reliable electric service with minimum impact on the environment, and (3) the Department's electric industry restructuring principles and proposal. The Department found that the provisions of the Settlement that were a condition of its approval represented, on balance, a just and reasonable resolution of restructuring issues for the Company and its ratepayers, and therefore, were in the public interest. Id. In this review, the Department must determine whether the Amended Settlement is consistent with Department precedent and the public interest. Specifically, the Department addresses the divestiture of NEP's generating facilities prior to the retail access date, and the determination of costs to be recovered in both the fixed and variable components of the CTC.

In D.P.U. 96-25, at 27, the Department noted that the Settlement provided for voluntary divestiture of NEP's generation assets, with a return of the proceeds from divestiture to

customers as a credit against stranded costs. The Department found that proceeds from the divestiture of NEP's generating facilities, together with renegotiation of power purchase contracts, would provide an opportunity for significant reductions to the total amount that would otherwise be collected through the CTC. Id. The Department stated that mitigation of the CTC through methods such as divestiture would reduce or eliminate the need for deferrals of payments to suppliers for standard offer service. Id. n.41. The Department also found that the Settlement's provisions for the recovery of the CTC are consistent with the Department's restructuring principle to honor existing commitments, while requiring maximum mitigation of the stranded costs. Id. at 28.

The Amended Wholesale Settlement provides for the divestiture of NEP's generating facilities prior to the retail access date.¹² While the Companies are not required to solicit competitive suppliers for standard offer service, except for service after the retail access date, the Companies would receive the residual value credit from divestiture prior to the implementation of retail access. Because the divestiture plan is subject to Department review and approval, the Department would have an opportunity to review the divestiture plan, including the residual value credit. Therefore, the Companies' customers would receive the benefits of divestiture prior to retail access without creating a deferral of NEP's supplier costs.

¹² A consequence of divestiture prior to the retail access date is that the Companies would declare the wholesale access date. On the wholesale access date, the Companies (1) terminate their obligation to purchase all-requirements service under Tariff No. 1, and (2) purchase service at standard offer prices during the transition period between the wholesale access date and retail access. The Amended Settlement makes no provision for service from NEP to the Companies after the transition period.

The Department finds that divestiture of NEP's generating facilities prior to the retail access date is consistent with the Department's restructuring principle to honor existing commitments, while requiring maximum mitigation of the stranded costs.

In D.P.U. 96-25, at 26, the Department also noted that the Settlement provided for recovery of costs associated with nuclear decommissioning and site restoration; above-market payments to power suppliers; credit for unit sales contracts; above-market fuel transportation; payments in lieu of property taxes; damages, costs, or net recoveries from claims from third persons; performance-based rates for nuclear units remaining after market valuation; and employee severance and retraining. The Department found that the amount determined to be reasonable for these costs should be included in the variable component of the CTC, and the reasonableness of these costs would be subject to the informal dispute resolution procedures of the wholesale rate stipulation and agreement. Id.

The Amended Wholesale Settlement removes nuclear costs independent of operation from the fixed component and includes these costs with the decommissioning costs of the variable component. In addition, the Amended Wholesale Settlement requires purchasers of NEP's generating business to pay \$85 million of the costs for employee severance and retraining. The Amended Wholesale Settlement limits recovery of costs for employee severance and retraining to the amount to be paid by purchasers, except in the event of legislation changing required benefits, and provides for recovery of amounts actually incurred that are less than the \$85 million through the reconciliation account. The Amended Wholesale Settlement also defines responsibility for environmental response costs that may be incurred after

divestiture.

In D.P.U. 96-25, at 26 n.38, the Department recognized that the individual amounts for the variable component of the CTC had not been determined. The Amended Wholesale Settlement provides for a more accurate determination of these costs. The Department finds that the modifications to the calculation of the fixed and variable components are consistent with the Department's restructuring principles to honor existing commitments and ensure benefits to ratepayers.

With respect to the concern raised by Enron, the Department has already approved the reconciling mechanism, including the variable component of the CTC. Id. at 31. The Amended Wholesale Settlement modifies the reconciliation adjustment provision by limiting the annual adjustment to 0.2 cents per KWH and provides a return on any unamortized balance. In addition to providing stability to the CTC, the modification is consistent with the reconciliation mechanism approved by the Department in D.P.U. 96-25.

With respect to the concern raised by Wheelabrator, the Department stated that the financing requirements needed to implement a divestiture plan were not known and would depend on the proceeds of the sales and the structure of the transactions. Id. at 28. The financing requirements of the divestiture plan and assignment of the CTC are not before the Department at this time. As with the Wholesale Settlement, the Amended Wholesale Settlement does not provide for the assignment by NEP of all or a portion of the proceeds from the CTC. The Amended Wholesale Settlement does provide for NEP to reflect the annual effect of refinancings, repurchases, and retirements of securities following divestiture or securitization

associated with the implementation of the CTC.

The Department finds that the conditions of the Amended Settlement before us for approval continue to be consistent with (1) our primary objective to reduce costs, over time, for all consumers of electricity, (2) our goal to develop an efficient industry structure and regulatory framework that minimize costs to consumers while maintaining safe and reliable electric service with minimum impact on the environment, and (3) the Department's electric industry restructuring principles and proposal. Therefore, the Department finds that the conditions of the Amended Settlement continue to represent, on balance, a just and reasonable resolution of restructuring issues for the Company and its ratepayers, and thus, are in the public interest. Accordingly, pursuant to our authority to regulate the operations of the electric utility companies in Massachusetts under G.L. c. 164, ' ' 76 and 94,¹³ the Department approves the following provisions, which are conditions of the Amended Settlement:

- ' I. Price Reductions for All Customers, including (A) the unbundling of rates through the retail access date, (B) retail delivery rates and the standard offer effective from the retail access date through December 31, 2004, and (C) the right to file for a rate change in the event that the retail access date has not occurred by January 1, 2001;
- ' II. Benefits of Competition Extended to All Customers, provisions for (A) prior commitments with customers, and (B) the implementation of retail access;
- ' III. Protect the Environment and Promote Conservation, including (A) siting reform, (B) emissions reductions, and (C) conservation and load management, and renewables;
- ' IV. Protect Low-Income Customers, including the continuance of the low-income customer discount, funding of low-income customer DSM programs, and protection against redlining;

¹³ See also D.P.U. 96-100, at 22-23 n.16, n.17, 231-234, 264-268; D.P.U. 95-30, at 33-34, 40-44.

' V. Creation of a Fully Functioning Stable and Reliable Structure for the Competitive Market provisions that include (C) the separation of generation and transmission properties and facilities, (D) divestiture of NEP's generating facilities, and (G) unbundled distribution services;

' VI. Successors and Assigns, including the rights and obligations imposed on any signatory to the Revised Amended Settlement;

' VII. Additional Provisions, concerning the protection of settlement negotiations and the precedential effect of the Revised Amended Settlement.

As with the Department's approval of the Settlement, the Department does not act on the terms and conditions of service under retail delivery rates (Exh. MECo-1, vol. 3, Att. 4), and the terms, conditions, and settlement process with suppliers under retail delivery rates (id. Att. 9, see also ' V. Creation of a Fully Functioning Stable and Reliable Structure for the Competitive Market (F) customer service standards). These are not conditions of the Amended Settlement and will be addressed in D.P.U. 97-65. The performance standards under retail delivery rates are binding on the Company, unless generic standards that are more stringent are approved by the Department (November 7, 1996 Procedural Conference, Tr. at 21-22, citing Exh. MECo-1, vol. 3, Att. 7). In addition, the Department does not act on the provisions of ' V that include (A) regional reform (Exh. MECo-10, at 28, citing Exh. MECo-1, vol. 3, Att. 11), (B) the jurisdictional separation between transmission and distribution (id. citing Exh. MECo-1, vol. 3, Att. 12), (E) standards of conduct (id. at 35, citing Exh. MECo-1, vol. 3, Att. 14), and (F) customer service standards (id.). These are not conditions of the Amended

Settlement and were addressed in D.P.U. 96-25 (Phase II).¹⁴

As with the Department's approval of the Settlement, failure by the FERC to approve the Amended Wholesale Settlement, as filed, would render the Amended Settlement null and void, and of no effect. Approval of the Amended Settlement, unless otherwise agreed to by the Department, is limited to the provisions of the Amended Wholesale Settlement, as filed. FERC approval of provisions to the Amended Wholesale Settlement other than as filed with the Department, would require that the Amended Settlement be resubmitted for Department review.

VI. ORDER

Accordingly, after due notice and consideration, it is

ORDERED: That the provisions of the Amended Settlement listed as conditions in Section V, submitted to the Department on May 28, 1997, be and hereby are APPROVED; and it is

FURTHER ORDERED: That the tariffs submitted on May 28, 1997: M.D.P.U. Nos. 945-C through 951-C, 952-B through 957-B, 958-C through 961-C, 962-A, and 963-A for unbundled electric service for Massachusetts Electric Company; 964-C through 974-C, 977-C, and 978-B for retail delivery service for Massachusetts Electric Company; M.D.P.U. Nos. 392,

¹⁴ The Department's Order in D.P.U. 96-25 (Phase II) is not affected by the Amended Settlement.

399-B through 409-B for unbundled electric service for Nantucket Electric Company; and 410-B through 422-B, and 423 for retail delivery service for Nantucket Electric Company, be and hereby are APPROVED; and it is

FURTHER ORDERED: That the tariffs of Massachusetts Electric Company and Nantucket Electric Company for retail delivery service shall apply to electric service consumed on or after the retail access date, unless otherwise ordered by the Department.

By Order of the Department,

John B. Howe, Chairman

Janet Gail Besser, Commissioner